

## AMERICAN TRADE POLICY

## Throwing sand in the gears

WASHINGTON, DC

**The prospect of a trade war over bananas merely confirms other signs that protectionist pressure is rising in America. There is little hint of the determined political leadership needed to resist it**

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“I ISSUE a call to the nations of the world to join the United States in a new round of global negotiations to expand exports . . . We must tear down barriers, open markets and expand trade.” Stirring stuff from a president on trial: Bill Clinton in his state-of-the-union address to Congress on January 19th. Thankfully, it seems, at a time when the world economy looks fragile, America is taking the lead in fighting to open the markets that many would like to shut.

If only. Mr Clinton also promised to retaliate “when imports unlawfully flood our nation.” “I have already informed the government of Japan that if the nation’s sudden surge of steel imports into our country is not reversed, America will respond,” he said, to the loudest cheers of the night from assembled congressmen. A week later, the administration also won acclaim when it promised to revive “super-301”, a trade law authorising retaliation against countries that America deems to be unfairly blocking imports.

Even more immediately, America is on the brink of a trade war with Europe over bananas. Unless a compromise is reached this weekend, the United States could on February 1st slap 100% duties on a wide range of European imports, from pecorino cheese to cashmere sweaters, in a battle over the European Union’s banana import rules. The World Trade Organisation has ruled that these discriminate in favour of Caribbean banana producers and against American distributors, especially Chiquita, an Ohio-based firm that is a big campaign-finance contributor. The EU has since modified its regime, but the Americans say it still breaches WTO rules. Since they suspect the EU is merely foot-dragging, they say their proposed sanctions are legal.

In short, trade, after some years on the back-burner, is back on America’s political agenda—but for all the wrong reasons. Surging imports from crisis-hit economies in Asia and elsewhere have triggered demands for protection from steel makers and others. Countervailing voices calling for markets to be kept open have been depressingly weak. Exporters are disenchanted because sales are shrinking. Popular support for free trade is low and has fallen in recent years. And neither Mr Clinton nor Congress seems willing to go out on a limb for free trade in the year before a presidential election. So when America’s economy slows, as it will surely do later this year, the pressure for protection may be overwhelming—and the

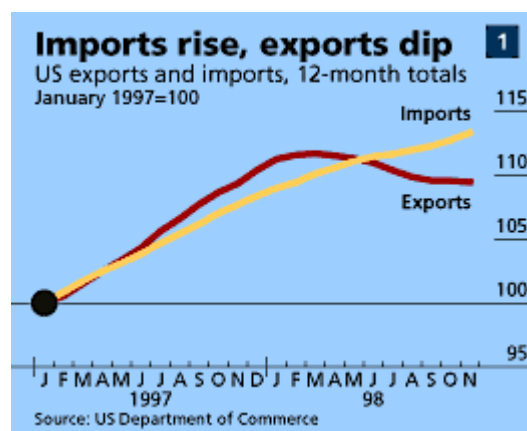
world's financial turmoil could turn into a general trade war.

What of Mr Clinton's high-flown rhetoric about a new round of trade liberalisation? It is largely empty. True, America is hosting a big WTO meeting, probably in San Diego, later this year. And now that it has warmed to the idea—which others, notably the EU, have long championed—a trade round could be kicked off there. Yet the public and Congress are sceptical; and America's agenda is still undefined. Most important of all, Mr Clinton does not have the means to negotiate credibly: "fast-track" authority, which allows him to strike trade deals that Congress must accept or reject, but cannot amend.

### The protectionist peril

Although America is still booming, demand is falling in much of the rest of the world. So companies are exporting more to America instead. In some industries, notably steel, which already had excess capacity, their efforts have been frantic. Asian, Russian—and now Brazilian—firms have gained a competitive edge from falling exchange rates. Not surprisingly, their American rivals are not amused.

Exporters are grumbling too. The rest of the world's economic troubles have hit American exports hard (see chart 1). Despite a weakening dollar, Goldman Sachs expects American exports to fall this year for the first time since 1983. Boeing, America's largest exporter, has recently announced massive lay-offs. Ominously, America is now taking aim at Airbus, Boeing's European rival, in a repeat of the dispute over subsidies that almost triggered a trade war in 1992.



With imports surging and exports on the slide, America's trade deficit is soaring. The visible-trade gap ballooned to a record \$244 billion in the year to November (see chart 2). It is bound to get even bigger, because America's economy is growing faster than the rest of the world's and American savings continue to be low or even negative. Yet politicians are seizing on the trade gap as a sign that foreigners are competing unfairly. America's trade supremo, Charlene Barshefsky, sees the deficit reaching \$300 billion this year, a level she calls "politically unsustainable".

When the American economy slows, companies will feel even more squeezed by cheaper imports. As unemployment rises from its current lows, the protectionist constituency is sure to grow, just as it has done in previous slowdowns. What is worryingly different this time is that the outbreak of protectionism in America has

started while the economy is still strong.

True, some exporters will resist any measures that invite foreign retaliation. And companies that buy supplies abroad will fight anything that raises their costs. Caterpillar, a tractor maker, has come out against imposing quotas on foreign steel. Robert Rubin, the Treasury secretary, has said that America must keep its borders open to imports from crisis-hit economies so as to ward off the threat of world recession. Moreover, world trade rules may deter America from erecting import barriers.

But these constraints are far from fail-safe. Producers threatened by imports are concentrated, organised and vocal; those who benefit from trade are diffuse and their stake in any specific case is usually small. Industries such as steel have huge political clout. And since exports are also shrinking, the free-trade lobby is weaker than usual. Moreover, many companies that buy abroad are loth to speak out for free trade now in case they want protection later. General Motors, a big steel user, has failed to stand up to the steel lobby.

Politicians are unlikely to put up much of a fight for free trade either. Republicans are divided and see few votes in taking a stand for free trade. Most Democrats sympathise with protectionist arguments. Many in Congress are beholden to trade unions for campaign contributions. Bill Daley, the commerce secretary, is lobbying furiously for a tougher line on imports. He urges companies to make anti-dumping authorities “the busiest people in town”. Ms Barshefsky is only slightly more measured. As for Mr Clinton, he has yet, even in an unprecedented peacetime boom, to confront the protectionist arguments head-on. He is unlikely to do so now next year’s elections are drawing nearer.

What of world trade rules? For a start, they allow some protectionist measures, notably “anti-dumping” duties on imports that are deemed unfairly cheap. America could also defy world trade rules, at least until the WTO forces it to mend its ways, which can take several years. Countries that are not WTO members, such as China, Taiwan and Russia, are especially vulnerable to trade sanctions because they do not have the protection of the WTO.

### **Creeping up**

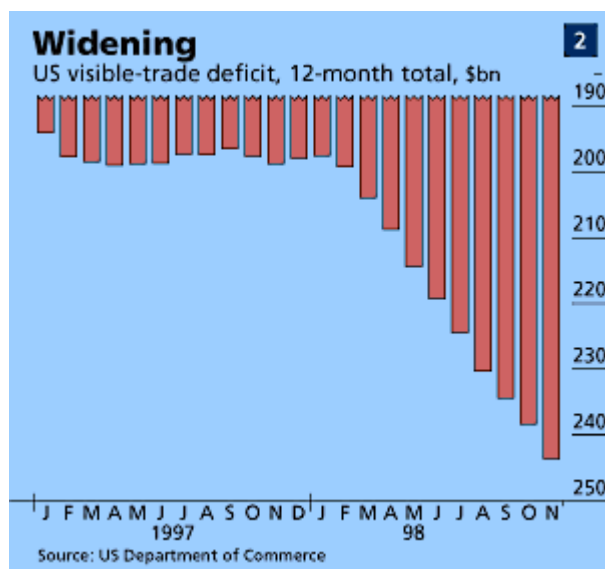
A wholesale retreat behind tariff barriers is unlikely. But a creeping rise in protection is on the cards. “It will be like throwing a lot of sand in the gears, rather than putting a monkey-wrench in,” argues Jeffrey Garten, dean of the Yale School of Management.

Already, there has been a surge in anti-dumping cases. Twenty-seven investigations were launched last year, up from 16 in 1997. Many more are in the offing this year. The steel industry, which is currently seeking relief from Japanese, Russian and Brazilian imports, is threatening a slew of new cases, notably against South Korea. Duties have been slapped on South Korean memory chips; those from Taiwan are now being targeted. Cases are pending in machine tools, textiles and clothing, and even apple juice.

The threat of anti-dumping duties is spurring some foreigners to cut their exports. Japanese steel producers have unofficially agreed to reduce their exports to America to their level before the Asian crisis. The volume of Japanese steel exports to America fell by 14% in December, the first monthly decline in 33 months. Mr

Clinton says America plans to monitor steel imports monthly to make sure Japan continues to comply. South Korean steel makers say they will curb their exports unilaterally in a bid to avoid a clash with America. Such “voluntary export restraints” are likely to proliferate. Though they are illegal under world trade law, it would be hard—and in any case take a long time—to strike them down at the WTO without evidence of a formal agreement between governments.

The steel industry is also pursuing another path to protection. Through huge rallies in steel-belt states and advertisements urging Americans to “Stand Up for Steel”, it is lobbying Congress to change the law to make it easier to get protection from imports. Their many demands include closer import monitoring, tighter anti-dumping laws and easier provisions for temporary safeguards against import surges.



The administration has already made concessions. It is speeding up anti-dumping applications and promising retroactive penalties on imports. On January 7th the White House offered steel makers a subsidy package that includes \$300m of tax breaks. It is under great pressure to go further. “The White House will definitely give them something,” says Craig VanGrasstek, a specialist on American trade politics. If—as seems likely in the current climate—that involves changing the law to help steel makers, other industries will take advantage of the new provisions too.

These wrangles over steel could turn into a full-blown trade war with both Japan and the EU. America is not alone in its reluctance to allow ailing firms to go to the wall; European and other producers want help too. The EU, for instance, is pursuing 13 steel anti-dumping cases; many more are in the pipeline. It is easy to imagine a tit-for-tat war involving anti-dumping, subsidies, quotas and the like. Indeed, the EU is considering challenging America’s new steel subsidies at the WTO.

More broadly, America growls that the EU and Japan are not doing their fair share to absorb rising imports from Asia and elsewhere. Ms Barshefsky went to Tokyo earlier this month to lecture the Japanese. Mr Clinton has threatened “retaliatory protectionism” unless the Japanese do more to open their markets. But America’s

complaints have met with hostility. “Feelings between America and Japan are as bad as I’ve seen them,” says Mac Destler, a specialist in American trade politics at the University of Maryland.

Relations with the EU are also prickly. The banana war could soon become a beef war as well, as the WTO has ruled against the EU’s ban on hormone-treated beef imports but the EU is making no effort to comply. America and the EU are also clashing over mobile-telephone standards and data privacy. The backdrop to all these disputes is that the EU no longer feels the need to play second fiddle to America on trade; it responds in kind to what it sees as America’s aggressive unilateralism.

Tension with China is rising too. America’s bilateral deficit with China, at \$57 billion in the year to November, is second only to its deficit with Japan. China exports five times as much to America as it imports. It is, moreover, an easy target for American sanctions, since it has enacted its own measures to curb imports and cannot appeal to the WTO against any American action. The flashpoint could be Congress’s annual vote in June on renewing normal trading relations with China, which will be swayed by its human-rights record. China could also be hit by a new law that allows the administration to impose sanctions on countries that persecute religious groups.

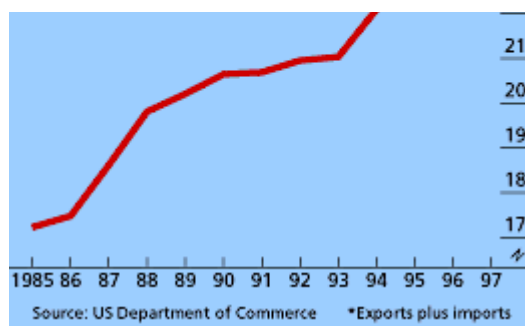
A new round of trade talks could, in theory, put the brakes on a slide into protectionism. The risk of disrupting delicate negotiations might deter the administration from giving in to protectionist demands; the prospect of new export markets would mobilise free-traders. But Mr Clinton will be constrained by lack of popular support for freer trade, which may make it impossible for him—or his successor—to win a usable fast-track mandate.

### The fall-out from NAFTA

The roots of Mr Clinton’s current difficulties lie in his first years in office. In 1993 Congress approved the North American Free-Trade Agreement (NAFTA). And in 1994 it passed the Uruguay round of the GATT, a huge multilateral trade-liberalisation package that gave birth to the WTO, complete with a mandate to enforce world trade laws. These were landmark achievements. But they came at a substantial cost.

NAFTA, in particular, was passed only after a bruising battle. To win over reluctant Democrats in Congress, side-agreements were tacked on to meet concerns that free trade with Mexico would encourage companies to move south of the border to take advantage of weaker labour and environmental standards. But these annoyed many free-traders, especially businessmen and Republicans. When Mr Clinton asked a now Republican-controlled Congress to renew fast-track authority in 1994, it said no—as it did in 1997 and last year, although the administration did not push hard on these occasions.





Getting the Uruguay round through Congress was equally tortuous. A major sticking-point was the fear that the WTO infringes on American sovereignty, since it is the only international body whose rulings America cannot veto. For right-wingers, the WTO conjured up fears of a world government usurping America's. For the left, it threatened to override American rules on such sensitive issues as environmental protection or product safety. The vote was won, but with the proviso that Congress can withdraw from the WTO if it thinks the organisation is exceeding its authority or acting "arbitrarily or capriciously".

America's economy now has greater links with the rest of the world: exports and imports were together equivalent to 25% of GDP in 1997, up from 21% in 1993 and 17% in 1985 (see chart 3). Yet canny protectionists have focused fears about the pace and sweep of globalisation on to trade. The WTO, moreover, is increasingly unpopular. Its recent caseload has included such sensitive issues as America's sanctions on countries doing business with Cuba, Iran and Libya as well as its ban on shrimp imports from countries using nets that trap turtles. This has sharpened the fears of both left and right.

These concerns reinforce the political deadlock on fast-track. Even if Mr Clinton makes a concerted push for it, he is unlikely to win over the House of Representatives. Trade unionists and greens have hardened their demands. Partly because NAFTA's side-agreements have proved toothless in practice, they will now back fast-track only for trade deals that include tough and enforceable labour and environmental standards. They are also pressing for more active scrutiny by Congress during trade negotiations. Most Democrats—notably Dick Gephardt, House minority leader—are sympathetic to their concerns.

Mr Clinton cannot afford to ignore their views. He does not want to harm Vice-president Al Gore's presidential hopes in 2000 by alienating his core constituency. Mr Gore has gone out of his way to sound tough on trade recently, not least because he is worried about a challenge from the left, possibly from Mr Gephardt.

But Mr Gephardt's fast-track agenda is anathema to most businessmen, as well as to Republicans, who still have a majority in the House. They could conceivably push for a fast-track bill of their own that excludes labour and the environment. But it would be unlikely to garner enough votes because some Republicans oppose free trade. They are anyway loth to press fast-track, such is their dislike and wariness of Mr Clinton. Efforts by the Senate Finance Committee to push a broader trade bill that bounces the House into agreement also seem unlikely to succeed.

Without fast-track, Mr Clinton's trade policy is hamstrung. America cannot credibly negotiate big trade deals when there is a risk that Congress may amend

them or impose labour and environmental provisions that other countries are unwilling to tolerate. Mr Clinton's plans for freer trade in the Americas have already stalled because he does not have fast-track. It dims prospects for a new WTO round too.

Some have argued that fast-track is needed only to finish a round, not to start it. After all, the Uruguay round was started without it in 1986. But 1999 is not 1986. Then, Congress had never rejected or sought to impose conditions on fast-track; nobody doubted it would eventually be granted. Now, few think it could be before 2001. Such uncertainty will make other countries reluctant to make firm negotiating commitments. It is also a perfect excuse for them to drag their feet. Moreover, even if fast-track did somehow pass, it would probably include labour and environmental provisions that most of America's negotiating partners strongly oppose. Such a fast-track mandate "would destroy any possibility of negotiation", according to Sylvia Ostry of the University of Toronto, a former Canadian trade negotiator.

For the world at large, the drift of American trade policy is worrying. Rising protectionism invites retaliation. A deadlock on further liberalisation encourages backsliding. Emerging economies are already the biggest users of anti-dumping suits. Brazil, China and Russia have all recently tightened import controls. The protectionist instincts of the EU and Japan are undimmed. Over the past 50 years, America has led successive efforts to free world trade. Unless it reclaims that mantle, the prospects for keeping trade as free as it is, let alone for freeing it further, will remain grim.

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